254(b)(3) of the 1996 Act.

As discussed in question 3, the critical factor is the amount of cost remaining to be recovered after receipt of the universal service support. To the extent all or part of this remainder is recovered through end user charges, the charges must fall within a reasonable variation from the charges to urban users. Reasonable, in regard to local service rates, necessarily includes a consideration of calling scope. A $20 charge for a service that permits calling to 800 other subscribers is not comparable to a $20 charge that provides access to a million subscribers.

41. How should support be calculated for those areas (e.g., insular areas and Alaska) that are not included under the proxy model?

Actual cost should be used for all rural telephone companies and any non-rural LECs serving insular areas, Alaska or other high cost areas. Since the record shows that proxies are inaccurate for small and rural LECs, it would be discriminatory to allow only insular or Alaskan LECs to use reliable (i.e., actual) costs.

42. Will support calculated using a proxy model provide sufficient incentive to support infrastructure development and maintain quality service?

Investment incentives to modernize the infrastructure and maintain quality service will only be adequate to the extent that carriers believe they will have a fair opportunity of recovering the real costs of their real networks. As long as no proxy has been sufficiently validated and priced out to provide a secure level of confidence in its accuracy, the riskiness of investment will provide a strong disincentive.

Additionally, the current mechanism does contain an incentive to upgrade since it compensates the carrier after the infrastructure investment has been made. Unfortunately, a proxy

model will compensate a carrier, based on a hypothetical network, whether or not the carrier invests.

43. Should there be recourse for companies whose book costs are substantially above the costs projected for them under a proxy model? If so, under what conditions (for example, at what cost levels above the proxy amount) should carriers be granted a waiver allowing alternative treatment? What standards should be used when considering such requests?

If a proxy is adopted, it should allow relief at the option of the carrier for underpredictions of actual costs. The Joint Board should reject any proxy that has not been shown through reliable price outs to be valid for all the LECs to which it will apply. The universal service commitment in the Act and the deregulatory purpose of the legislation stand in the way of a system likely to require large numbers of waiver proceedings, thereby adding to the cost of universal service, without any gain over the current actual cost methodology for most ILECs.

44. How can a proxy model be modified to accommodate technological neutrality?

A proxy model based on a forward looking, imaginary network using "optimal" technology is by definition technologically biased in favor of the chosen technology and against other networks. Actual costs allow for differences in technology, while leaving the chosen technologies to compete against each other on the basis of their costs and technical advantages, is essential to allow the marketplace to select the technologies that meet their needs. Consequently, a proxy model, based on one theoretical network design, cannot adequately accommodate technical neutrality.

45. Is it appropriate for a proxy model adopted by the Commission in this proceeding to be subject to proprietary restrictions, or must such a model be a public document?

A model must be available without cost to those that will be affected if it is adopted. It would be a fatal procedural and substantive flaw to proceed without the information necessary for an affected business, including a small LEC, to evaluate the effect on its revenues. Also, the model needs to recognize individual companies' proprietary information.

46. Should a proxy model be adopted if it is based on proprietary data that may not be available for public review?

A company should not be required to make specific information about its own operations available to competitors, but a company should not be subjected to a costing mechanism that affects its revenues or how it may recover its high costs on the basis of a methodology that is too complex or inadequately disclosed for it to determine what the effects will be. Of course, individual proprietary information should remain confidential.

47. If it is determined that proprietary data should not be employed in the proxy model, are there adequate data publicly available on current book costs to develop a proxy model? If so, identify the source(s) of such data.

As indicated above, the test of whether a proxy is valid is not whether it has the right inputs, but whether it predicts what it purports to predict. The test of whether a proxy is useful is whether the predicted result meets the statutory objectives. Therefore the test of the adequacy of the data is whether, when used, both the validity and objectives tests are met.

48. Should the materiality and potential importance of proprietary information be considered in evaluating the various models?

See answers to questions 45, 46 and 47, above.

Competitive Bidding

49. How would high-cost payments be determined under a system of competitive bidding in areas with no competition?

The Act limits high cost compensation to state-designated essential telecommunications carriers (ETCs), § 214(e). If no competing ETC has been designated, there can be no other LEC to bid for the cost recovery. In a rural LEC service area, the state must make a public interest finding before it designates an additional ETC, § 214(e)(2), so Congress plainly did not have bidding for rural high cost support levels in mind.

In addition, the high cost mechanism must be "sufficient," so the single ETC in a non-competitive market would have to recover its excess costs, but must compensate no more than those costs, to avoid cross-subsidy forbidden by § 254(k). Therefore, the Act precludes bidding in a non-competitive area.

Specifically, § 254(b)(5) of the 1996 Act mandates "specific and predictable support mechanisms." Exposing high-cost customers to the vagaries of competitive bidding would not be predictable. Also, the lowest cost provider, in many cases, might not provide sufficient support.

50. How should a bidding system be structured in order to provide incentives for carriers to compete to submit the low bid for universal service support?

The Act also precludes competitive bidding for the support level in competitive markets. Again, state designation as an ETC is a prerequisite, so only a CLEC designated as an ETC could be a potential bidder. Even if multiple ETCs had been designated, the statutory requirement for "precise, sufficient and predictable" high cost recovery would not permit the bid of one LEC to set recovery levels for other ETCs. The losing bidder's high cost recovery, based on the low

bidder's bid, would not be specific to any of them. Nor would such recovery be "sufficient" for any of the losers.

Setting a winner's premium to induce low bidding would increase the statutory conflict. It would subsidize the winner by paying more than its bid indicated it needed, thus overloading the cost burden on the end users that will ultimately fund the universal service contributors, contrary to § 254(k).

Forcing under recovery by the losing ETCs and over recovery by the winning bidder would impede and could destroy the existing competition and the incentives for future competition.

Unlike the PCS auctions, where there were numerous interested parties, high-cost areas have historically been ignored by the larger carriers. Designing a complex and administratively burdensome bidding system, for an area that no one (with the exception of rural telcos) may want to serve, would be a challenge even to a team of game-theory economists.

51. What, if any, safeguards should be adopted to ensure that large companies do not bid excessively low to drive out competition?

The experience with the C-Band PCS auction shows that it is probably impossible to conduct something resembling an auction in which the highest (i.e. most service for the dollar) bidder does not prevail. This question illustrates the precise problem with the auction proposal: The excellent service at reasonable prices which small and rural companies now provide can be destroyed by any big company which wants to take over the area.

The best safeguard against gaming of the bidding by anyone would be to adhere to the high cost recovery framework Congress established and eschew competitive bidding. Indeed, it

is not clear why the Common Carrier Bureau is asking about competitive bidding in this expedited implementation proceeding. The Commission admitted in its earlier universal service proceeding that competitive bidding was not then feasible. There is no reason to think it is a feasible approach now, even if it were not also unlawful.

The PCS auctions demonstrated the difficulties of avoiding the deep-pocketed influence of large companies, even in the "entrepreneurs" blocks. This question illustrates one of many inherent flaws in the idea of competitive bidding. If a large company wants to "low-ball" bid for an area, it will be hard to stop. The resulting replacement of a small or rural carrier with a monolithic entity is contrary to the Act's pro-competitive slant.

52. What safeguards should be adopted to ensure adequate quality of service under a system of competitive bidding?

During the 1970's and 1980's large companies bid for municipal CATV franchises by promising to provide more services at lower cost than their competitors. In many cases the result was that as soon as the franchise was acquired, the cable company "discovered" it could not feasibly deliver what it promised and either sold out or negotiated its obligations down. The same result could occur in the telephone situation, with the added feature that the incumbents who took the initiative to invest in their communities would be destroyed.

Competitive bidding would under-compensate the losing competitors. They would, thus, have strong incentives not to maintain high service quality, especially in rural areas, let alone to invest in developing competing facilities-based competition. The winning bidder would also have an incentive to use its windfall high cost compensation to compete elsewhere, and not to maintain high service quality or investment where it hopes to continue as the low bidder.

Again, competitive bidding, by its very nature, contains a disincentive to invest in quality service, which is contrary to the Act's intent. This question exposes yet another inherent flaw in the auction proposal.

53. How is collusion avoided when using a competitive bid?

The RTC is strongly opposed to "auctioning" off universal service, but any auction rules should make collusion illegal.

54. Should the structure of the auction differ if there are few bidders? If so, how?

No comment.

55. How should the Commission determine the size of the areas within which eligible carriers bid for universal service support? What is the optimal basis for determining the size of those areas, in order to avoid unfair advantage for either the incumbent local exchange carriers or competitive carriers?

Even if bidding were lawful, the area used to determine universal service compensation and the ETCs' serving areas are the "service area" set by the State or the study area of a rural LEC until changed by a Joint Board. Therefore, the Commission should not try to encroach on the area designations Congress left for determination by others as intrinsic to the high cost recovery framework in the Act.

Benchmark Cost Model (BCM)

56. How do the book costs of incumbent local exchange carriers compare with the calculated proxy costs of the Benchmark Cost Model (BCM) for the same areas?

In previous comments, the RTC has noted that the for individual small companies, there can be no assurance the model will predict either its actual cost or the (forward looking) cost of

building a new network in its area using a hypothetical design. The sponsors of the BCM readily acknowledge this fact. NECA is currently analyzing the latest version of BCM and is expected to file its results on August 9, at which time the RTC also expects to have further comment.

57. Should the BCM be modified to include non-wireline services? If wireless technology proves less costly than wireline facilities, should projected costs be capped at the level predicted for use of wireless technology?

The RTC understands that the BCM model now includes an assumed cost level at which wireless loop technology would be used. The basis for this assumed level is not clear. Such assumptions cannot be made purely on a cost basis, however, because wireless technology is not universally available or usable.

58. What are the advantages and disadvantages of using a wire center instead of a Census Block Group as the appropriate geographic area in projecting costs?

On the one hand, wire centers can provide a realistic basis for determining actual costs below the study area level because they are a basic building block of the local network. On the other hand, for rural companies, wire center average cost as a basis for determining support which could be available to competitors provides inadequate protection from cream skimming. If a competitor can build (or convert CATV) facilities in a core area with relatively higher density and lower cost, and (if required) resell the incumbent's rural facilities at a wash, while receiving per line support at the average, the new entrant will receive a windfall, and the incumbent will be forced to raise prices to rural subscribers.

59. The Maine PUC and several other State commissions proposed inclusion in the BCM of the costs of connecting exchanges to the public switched network through the use of microwave, trunk, or satellite technologies. Those commenters also proposed the use an additional extra-

high-cost variable for remote areas not accessible by road. What is the feasibility and the advisability of incorporating these changes into the BCM?

Adding factors is a way to get closer to the variability of small and rural LECs' conditions and costs. However, more accuracy that comes at the cost of even greater complexity and administrative burdens and expenses will probably illustrate further that actual cost is preferable.

In any event, any modified proxy would need validation as an accurate predictor of costs for all the providers that would be expected to use it. The differences between ILECs and CLECs, cable, wireless and other competitors are undoubtably great. Specific mechanisms will require validation for all to avoid the competitive advantages and disadvantages that will inevitably arise from inaccurate cost methodologies.

The diverse variables that influence cost in areas not accessible by road are too numerous to mention (terrain, slope, weather, rocks, lower oxygen level...). Adding variables for different technologies such as microwave and satellite (will it be an Iridium proxy, a Teledesic proxy, or an Odyssey proxy?) to the not-accessible-by-road proxy would create a geometrically complex variable with a highly unlikely correlation to real world cost.

60. The National Cable Television Association proposed a number of modifications to the BCM related to switching cost, fill factors, digital loop carrier subscriber equipment, penetration assumptions, deployment of fiber versus copper technology assumptions, and service area interface costs. Which, if any, of these changes would be feasible and advisable to incorporate into the BCM?

See answer to question 59, above.

61. Should the support calculated using the Benchmark Cost Model also reflect subscriber income levels, as suggested by the Puerto Rico Telephone Company in its comments?

No. Income levels are relevant to low income programs (i.e., Lifeline and Linkup). The

combination of effective high cost mechanisms and effective low income programs -- which in each case must be "sufficient" to the universal service purposes, § 254(e) -- should be "sufficient" to deal with the low income concerns in Puerto Rico and elsewhere.

62. The BCM appears to compare unseparated costs, calculated using a proxy methodology, with a nationwide local benchmark rate. Does use of the BCM suggest that the costs calculated by the model would be recovered only through services included in the benchmark rate? Does the BCM require changes to existing separations and access charge rules? Is the model designed to change as those rules are changed? Does the comparison of model costs with a local rate affordability benchmark create an opportunity for over-recovery from universal service support mechanisms?

The required "sufficient" federal mechanism must fulfill the purposes of § 254. This will require high cost recovery that deals adequately with unseparated high costs. Indeed, today's USF provides interstate high cost recovery based on unseparated loop costs to prevent excessive cost shifts from raising local rates unduly. Congress did not enact the 1996 Act to increase customers' rates or diminish service quality and investment incentives.

63. Is it feasible and/or advisable to integrate the grid cell structure used in the Cost Proxy Model (CPM) proposed by Pacific Telesis into the BCM for identifying terrain and population in areas where population density is low?

This question must be addressed by the respective sponsors.

Cost Proxy Model Proposed by Pacific Telesis

64. Can the grid cell structure used in the CPM reasonably identify population distribution in sparsely-populated areas?

Same answer as for question 56.

65. Can the CPM be modified to identify terrain and soil type by grid cell?

See answer to question 59, above.

66. Can the CPM be used on a nationwide basis to estimate the cost of providing basic residential service?

Universal service is not confined to residential service. Indeed, when AT&T tried to convince the Conference to interject "residential" into § 254(g), the effort failed. If Congress had meant to limit universal service to residential service, it would have so stated.

67. Using the CPM, what costs would be calculated by Census Block Group and by wire center for serving a rural, high-cost state (e.g., Arkansas)?

Pacific should provide this information.

68. Is the CPM a self-contained model, or does it rely on other models, and if so, to what extent?

See above.

SLC/CCLC

69. If a portion of the CCL charge represents a subsidy to support universal service, what is the total amount of the subsidy? Please provide supporting evidence to substantiate such estimates. Supporting evidence should indicate the cost methodology used to estimate the magnitude of the subsidy (e.g., long-run incremental, short-run incremental, fully-distributed).

The RTC does not believe that the CCL or any significant part of it is a subsidy. It recovers legitimate costs from interexchange carriers that benefit from network costs incurred to accommodate their use. If the Joint Board, nevertheless, decides to change the CCL, the costs should not be dumped into the intrastate jurisdiction or loaded onto local exchange customers by major increases in the SLC. The RTC would not oppose a carefully limited increase in the SLC, so long as the burden on customers in high cost areas were not disproportionate and the shifted

costs were not permitted to deaverage CCL charges beyond today's disparity. To do otherwise would conflict with the Act's geographic averaging mandate for interexchange rates, § 254(g), and the policy of encouraging interexchange competition in rural areas: It would increase the pressure on IXCs that serve rural areas and further decrease the existing marketplace disincentives to provide competitive interexchange services in high cost markets.

To the extent the concern is recovery of NTS cost through a usage based charge so that large volume users pay more than low volume users, the intra-customer "subsidy" can be reduced or eliminated by changing the cost recovery plan to a non-usage based charge.

70. If a portion of the CCL charge represents a contribution to the recovery of loop costs, please identify and discuss alternatives to the CCL charge for recovery of those costs from all interstate telecommunications service providers (e.g., bulk billing, flat rate/per-line charge).

Bulk billing would be appropriate for the CCL because it recovers non-traffic sensitive costs. Recovering such costs through usage-based charges is likely to provide misleading market signals. A flat rate per line to the IXC would penalize the universal provision of interexchange services. However, an attempt to shift a sizable share of the costs into a SLC-type charge per line would conflict with the intent and expectations of Congress.

Low-Income Consumers

71. Should the new universal service fund provide support for the Lifeline and Link-Up programs, in order to make those subsidies technologically and competitively neutral? If so, should the amount of the lifeline subsidy still be tied, as it is now, to the amount of the subscriber line charge?

It would be reasonable -- and is doubtless required by the Act, § 254(d) (requiring contribution by all providers to federal universal service mechanisms) -- to recover the costs of

the Lifeline and Link-Up programs for low income customers from the broader pool of all interstate telecommunications providers. The new responsibility on the federal universal service mechanisms to provide "sufficient" support for the Act's universal service purposes may require farther reaching Lifeline and Link-Up support. Also, the Act clearly indicates that Lifeline and Link-Up are to remain separate.

Administration of Universal Service Support

72. Section 254(d) of the 1996 Act provides that the Commission may exempt carriers from contributing to the support of universal service if their contribution would be "de minimis." The conference report indicates that "[t]he conferees intend that this authority would only be used in cases where the administrative cost of collecting contributions from a carrier or carriers would exceed the contribution that carrier would otherwise have to make under the formula for contributions selected by the Commission." What levels of administrative costs should be expected per carrier under the various methods that have been proposed for funding (e.g., gross revenues, revenues net of payments to other carriers, retail revenues, etc.)?

The least administratively burdensome method of collection would be to simply have a $100.00 floor that every carrier must pay, similar to the TRS method. The Joint Board should set a minimum recovery for a provider with a specified minimum level of interstate retail revenues. All providers should pay at least this amount to relieve the smallest providers of administrative and calculation burdens. All providers with interstate retail revenues above the minimum would pay a given amount based on those revenues.

Respectfully submitted for the Rural Telephone Coalition,

By:

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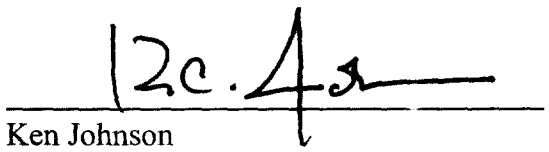

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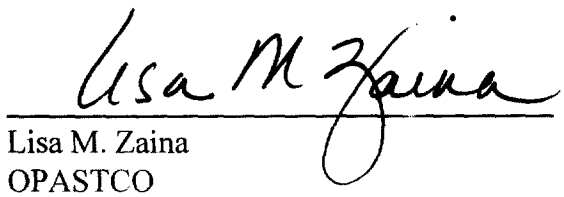

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CERTIFICATE OF SERVICE

I, Vanessa L. Fountain, hereby certify that a copy of OPASTCO's comments was sent on this, the 2nd day of August, 1996 by first class United States mail, postage prepaid, to those listed on the attached sheet.

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